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# AFFORDABLE OWNERSHIP HOUSING PROBLEMS AND OPTIONS

**A Background Paper**

**Prepared for**

**Development Services Department**
**Greater Vancouver Regional District**

**by**

**Clayton Research Associates Limited**

**May, 1990**

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## EXECUTIVE SUMMARY

This background paper is intended to educate and to stimulate public discussion on: the nature of the ownership affordability problem in the Greater Vancouver Area and its ramifications; the underlying causes of the problem; and the strengths and weaknesses of alternative government actions. It focuses on the difficulties that prospective first-time buyers are having in entering the homeownership market. It also concentrates on the affordability of existing homes since the bulk of first-time buyers buy a resale rather than a newly built home.

There is no question that the Greater Vancouver Area has a serious affordability problem in comparison with other major centres across Canada with the exception of Toronto. Moreover, affordability has steadily and dramatically deteriorated over the past three years. Rising home prices have been the most important factor in this deterioration of affordability though more recently rising mortgage interest rates have become an important factor as well.

An examination of ownership affordability has to recognize the wide variation in home prices throughout the Greater Vancouver Area. More affordable housing is to be found in suburban locations such as Surrey and Langley and in higher-density housing forms like townhouses and condominium apartments. Use of regional averages tends to mask the availability of this more affordable housing.

The simple reason for home prices rising so sharply is that the demand outpaced the supply. But this begs to question why the demand increased so rapidly and why the supply failed to keep pace. On the demand side, both the ownership and rental sectors of the housing market in the Greater Vancouver Area have been characterized by strong demand pressures since 1987 resulting from a strengthening economy.

The reason why the supply of ownership housing has not responded more to the surging demand is that two important factors of production (labour and land) have been in short supply. A shortage of labour is not as serious as a shortage of serviced land since higher compensation (wages, bonuses, etc.) attracts additional supply (through overtime, migration of construction workers to the Greater Vancouver Area). An increase in the supply of serviced land onto the market is largely in the hands of municipalities.

The land supply side of the market has not responded more to the demand pressures for a number of reasons including myopic expectations (the inability to anticipate or plan for an improved housing market), and inherent lags in the process for bringing serviced land onto the market. Community concerns about the effect of rapid growth on the quality of services in suburban municipalities is a contributor as well. Increasing financial requirements and regulations by municipalities on the developers of serviced land is adding to the cost base of land over the longer term.

The primary focus of municipalities to enhance the affordability of homeownership should be on the supply side of the market. Measures like a tax on investors/speculators or subsidies to first-time homebuyers do not attack the fundamental problems - a shortage of affordable homes. Initiatives that could be

undertaken by municipalities with the greatest potential for dealing with the problems include the following:

- Designating/zoning substantially more land for housing;
- Undertaking and following through with longer-term anticipatory planning;
- Shifting a large share of the financial burden of growth-related infrastructure from the shoulders of developers and suburban municipalities either through provincial grants and/or a restructuring of the property tax system to give suburban municipalities greater access to regional tax revenues from commercial and industrial assessment.
- Increasing the intensity of residential land use by reducing lot sizes for single-detached houses, allowing more semi-detached and townhouse units in new subdivisions and promoting more innovative land use configurations (e.g., cluster housing).
- Letting the market determine the appropriate densities for new housing rather than dictating densities.
- Allowing the conversion of existing rental buildings to owner-occupancy under a regime of controls which protect both existing tenants and the buyers of converted units.

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# 1.0 INTRODUCTION

There is no question that the affordability of ownership housing is a major issue in the Greater Vancouver Area. The dramatic reduction in affordability since 1987 in particular affects prospective first-time buyers.

## 1.1 PURPOSE OF THIS BACKGROUND PAPER

Government actions armed at mitigating this affordability problem should be based on an understanding of its causes and the relative advantages or limitations of various possible actions.

This background paper is intended to educate and to stimulate public discussion on:

- The nature of the ownership affordability problem in the Greater Vancouver Area and its ramifications;
- The underlying causes of the problem; and
- The strengths and weaknesses of alternative government actions.

## 1.2 SCOPE

The paper focuses on the difficulties that prospective first-time buyers are having in entering the homeownership market. This is not to imply that existing homeowners do not have any affordability difficulties, but, prospective first-time buyers have the dual problem of coming up with a sufficient downpayment as well as having sufficient income to meet the high cost of owning a home. The bulk of existing homeowners either have their mortgage paid off or have accumulated substantial equity and have higher incomes than they did at the time they purchased their home.

The paper concentrates on the affordability of existing homes since the bulk of first-time buyers buy a resale rather than a newly built home.

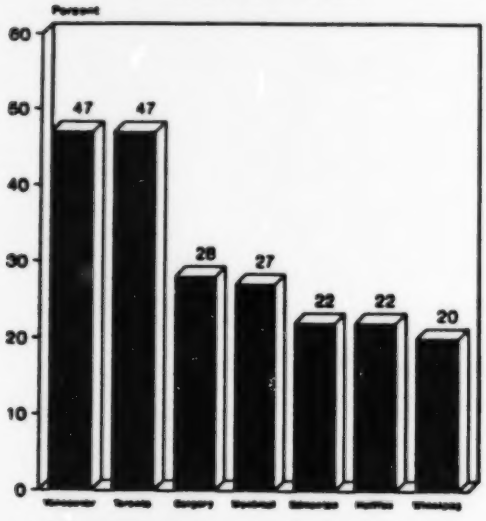
The paper's content is largely based upon a review of existing literature and readily available statistical information. These sources have been supplemented by "key informant" interviews.

## 1.3 CONTENTS

The paper has three main sections which coincide with the three topics outlined above in section 1.1.

**EXHIBIT 1**

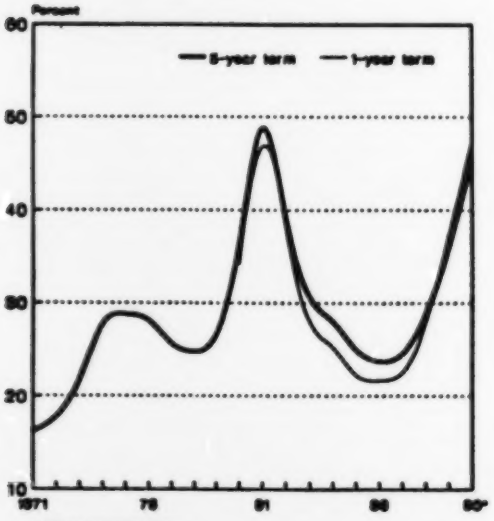
**PERCENT OF AVERAGE FAMILY INCOME REQUIRED TO BUY AN AVERAGE-PRICED MLS HOME, SELECTED URBAN CENTRES, FIRST QUARTER, 1990**




Source: Estimates by Clayton Research Associates based on data from the Canadian Real Estate Association, the Bank of Canada, and Statistics Canada.

**EXHIBIT 2**

**PERCENT OF AVERAGE FAMILY INCOME REQUIRED TO BUY AN AVERAGE-PRICED MLS HOME, GREATER VANCOUVER AREA, 1971-1990**




* First quarter only.

Source: Clayton Research Associates based on data from Statistics Canada, the Bank of Canada, and CREA.

# 2.0 THE NATURE OF THE AFFORDABILITY PROBLEM AND ITS RAMIFICATIONS

This section presents an analysis of both the nature of the homeownership affordability problem in the Greater Vancouver Area and its consequences. The chapter is divided into three major sub-sections:

- The seriousness of the current affordability problem;
- Identification of groups most affected by the lack of affordable ownership housing; and
- A description of the ramifications of the current ownership affordability situation.

## 2.1 HOW SERIOUS IS THE AFFORDABILITY PROBLEM?

### 2.1.1 Affordability Vis-À-Vis Other Major Urban Centres.

There is a serious homeownership affordability problem in the Greater Vancouver Area in comparison with other major centres across Canada, with the exception of Toronto (see Exhibit 1). The proportion of an average family's income required for annual mortgage payments on an average-priced MLS resale home in both the Greater Vancouver Area and Toronto currently exceeds 45 percent, assuming a 20 percent downpayment and a five-year term mortgage.

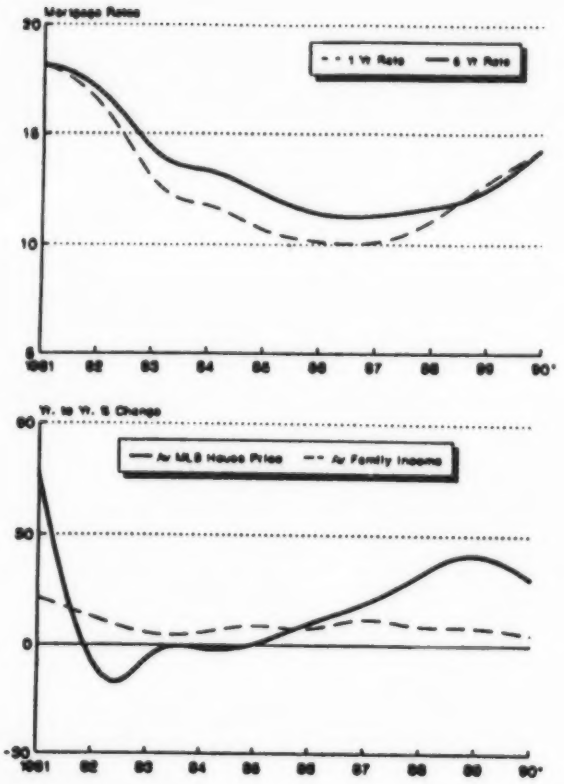
The access to homeownership in other major urban centres is far less restricted. Homeownership affordability is not much of a problem in either Edmonton, Winnipeg or Halifax - families need only dedicate 22 percent or less of their income on average to buy an average-priced MLS home. The average-priced MLS home is somewhat less affordable in Montreal and Calgary (27 and 28 percent mortgage payment to income ratios) but compared to the Greater Vancouver Area, homeownership in these centres is still very affordable.

### 2.1.2 Affordability Trends in the Greater Vancouver Area Over Time

Housing affordability in the Greater Vancouver Area has steadily and dramatically deteriorated over the past three years (see Exhibit 2). The proportion of an average family's income required to purchase an average-priced resale home in the Greater Vancouver Area has risen sharply from a fairly reasonable 23.5 percent in 1986 to an estimated 47 percent in early 1990 - a doubling in the affordability indicator. Homeownership in the Greater Vancouver Area has become less affordable than at any other time in the past two decades, with the exception of the year 1981 when the Greater Vancouver Area experienced its most severe ownership affordability crunch.

EXHIBIT 3

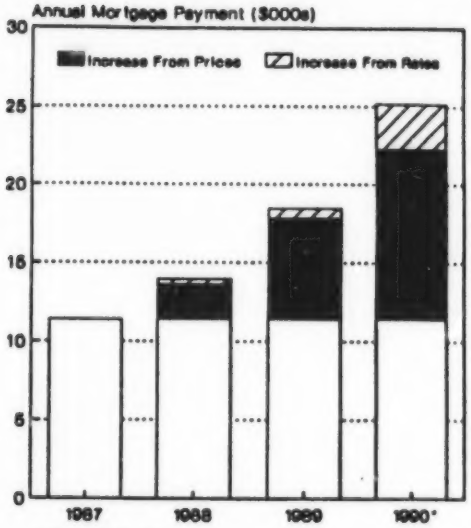
## COMPONENTS OF OWNERSHIP AFFORDABILITY, GREATER VANCOUVER AREA, 1981-1990




* First quarter only.
Source: Clayton Research Associates based on data from Statistics Canada and CREA.

EXHIBIT 4

## CONTRIBUTION OF RISING MLS HOME PRICES AND INTEREST RATES TO THE RECENT DETERIORATION IN AFFORDABILITY




* first quarter only.
Source: Clayton Research Associates based on data from CREA and Statistics Canada.

The affordability of homeownership has over the past two decades followed a cyclical pattern. This past behaviour of affordability offers some insight into where homeownership affordability could be heading in the future. The Greater Vancouver Area has experienced two complete cycles in affordability over the past two decades and appears to have reached the peak of its third. Therefore, if history repeats itself, there will be some easing of affordability in the coming years.

### 2.1.3 Components of Affordability

Assuming a downpayment that is constant as a proportion of purchase price, ownership, housing affordability is the product of three major variables: home prices, interest rates and income. Changes in any of these variables can affect ownership affordability.

Mortgage interest rates steadily declined between 1981 and 1987, with the exception of an increase in 1984 (see Exhibit 3). However, more recently mortgage rates have drifted steadily upward. The five year conventional mortgage rate has increased to 14.25 percent in April of this year from 11.20 percent as recently as in 1987 (the average for the year as a whole).

Resale home prices in the Greater Vancouver Area remained relatively stable over the mid-1980s after taking a nosedive in 1982. More recently, home prices have increased significantly. The average-priced MLS home sold for $109,565 in 1986 and sold for $219,916 in March of this year; more than a 100 percent increase.

Average family incomes in the Greater Vancouver Area have increased throughout the past decade. However, the year-to-year percentage increases have exhibited substantial variability, with family income showing substantial gains in both 1985 and 1987. More recently, income increases have been modest and on a much smaller scale than increases in home prices.

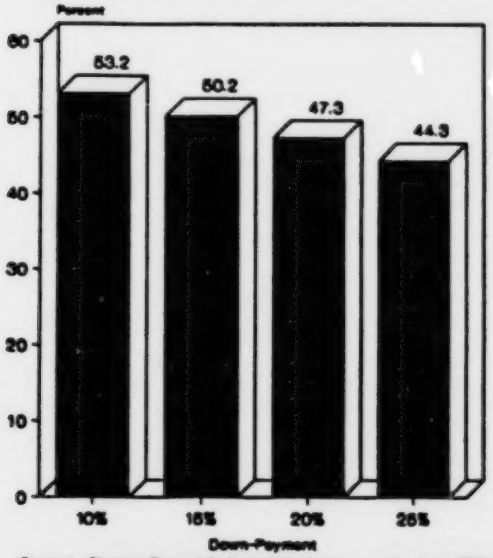
The combination of relatively low mortgage interest rates, in particular, but also increasing family income and stable home prices led to a significant improvement in the affordability of homeownership over the 1983 to 1987 period. More recently, however, dramatic increases in home prices and mortgage interest rates, combined with slower income growth, has led to a rapid deterioration of ownership affordability in the Greater Vancouver Area.

### 2.1.4 Relative Contribution of Higher MLS Home Prices and Rising Interest Rates to Sharp Deterioration in Affordability Since 1987

The dramatic deterioration in the affordability of homeownership over the past three years is a consequence of both increasing home prices and rising mortgage interest rates (see Exhibit 4). The annual mortgage payment required to purchase an average MLS house in the Greater Vancouver Area has increased from $11,416 in 1987 to

EXHIBIT 8

PERCENT OF AVERAGE FAMILY INCOME REQUIRED TO BUY AN AVERAGE-PRICED MLS HOME WITH DIFFERING DOWN PAYMENTS GREATER VANCOUVER AREA, 1ST QUARTER 1990




Source: Clayton Research Associates based on data from CREA and Statistics Canada.

$25,165 in early 1990 - an increase of 120 percent. Average family income has increased only 13 percent over the same period.

Mortgage payments increase if either home prices or mortgage interest rates rise. Both mortgage rates and home prices have been on the rise since 1987, but their relative contributions to the deterioration in ownership affordability have changed over time.

The annual mortgage payment on an average-priced resale home in the Greater Vancouver Area in 1988 was $2,539 higher than in 1987. Approximately 12 percent of this increase was due to higher mortgage rates while higher home prices contributed to most of the increase. Rising home prices continued to be the primary cause of the deterioration in ownership affordability in 1989, contributing to over 90 percent of the increase in annual mortgage payments from 1987. However, rising mortgage interest rates have become relatively more important to the deterioration in affordability. Mortgage interest rate increases made up 21 percent of the increase in annual mortgage payments required to purchase the average resale home in early 1990 over 1987 and 46 percent of the increase over 1989. Therefore, while rising home prices remain the most important factor in the deterioration of affordability, more recently rising mortgage rates have accounted for nearly half of the deterioration.

### 2.1.5 Sensitivity of Affordability to Differing Downpayment Ratios

The ratio of mortgage payments on an average-priced resale home to average family income is used extensively as a measure of the affordability of homeownership throughout the paper. This calculation assumes a 20 percent downpayment on the average-priced MLS home. Thus, the remaining 80 percent is financed with a mortgage. However, some prospective homeowners may be able to obtain a mortgage for up to 90 percent of the home value as many lending institutions with mortgage insurance will accept a 10 percent downpayment. Conversely, it may be the case that potential homebuyers (though fewer and fewer first-time buyers) have sufficient equity or savings to cover a downpayment larger than 20 percent of the home value. This section investigates the extent to which current affordability changes with varying downpayment assumptions.

The proportion of average family income required to purchase an average-priced resale home in the Greater Vancouver Area today is 47.3, assuming a 20 percent downpayment (see Exhibit 5). With a 15 percent downpayment the mortgage payment/income ratio increases to 50.2 - over half of average family income would be devoted to mortgage payments. These figures do not include transactions costs (appraisal fees, legal fees, property purchase tax) incurred when purchasing a home or ongoing costs (insurance, utilities, maintenance, property tax) faced by homeowners. Inclusion of these costs into the affordability calculations would reveal an even gloomier picture of the potential for homeownership with a low downpayment.

**EXHIBIT 6**
**VARIATIONS IN TYPICAL HOME PRICES BY UNIT TYPE AND AREA GREATER VANCOUVER AREA, APRIL, 1990**

| Area | Standard 2-Storey Single-Detached House | Standard Townhouse | Standard Condo Apartment |
|---|---|---|---|
| | | *Dollars* | |
| Port Coquitlam | n.a | 130,000 | 85,000 |
| Maple Ridge | 140,000 | 135,000 | 95,000 |
| Surrey | 150,000 | 123,000 | 100,000 |
| Langley | 185,000 | 105,000 | 90,000 |
| White Rock | 195,000 | 159,000 | 140,000 |
| North Delta | 205,000 | 120,000 | 130,000 |
| Tsawwassen | 225,000 | 135,000 | 115,000 |
| North Vancouver | 235,000 | 180,000 | 125,000 |
| Richmond | 235,000 | 151,000 | 115,000 |
| Coquitlam | 235,000 | 130,000 | 100,000 |
| Vancouver Eastside | 250,000 | 190,000 | 120,000 |
| Burnaby | 275,000 | 150,000 | 145,000 |
| Vancouver Westside | 380,000 | 280,000 | 265,000 |
| West Vancouver | 390,000 | 280,000 | 240,000 |

Source: Royal LePage.

With a downpayment of 25 percent of the current average resale home price of $219,916, the ratio of mortgage payments to average family income falls to 44.3. However, even with this larger downpayment, ownership housing costs comprise over 40 percent of the household's budget. In addition, it is unlikely that a significant number of households, especially potential first-time homebuyers, have $55,000 to use as a downpayment on an average-priced home. While they could buy a less, expensive home, the message is still the same - the Greater Vancouver Area has a very serious ownership housing problem.

### 2.1.6 Variations in Home Prices by Location and Housing Type

The average MLS resale home price data provide a good indication of home prices in the Vancouver area as a whole. However, there is a large degree of variability in home prices across municipalities and housing types which is masked by the MLS data which includes all types of resale housing - both less expensive and luxury. In looking at the affordability issue, it is relevant to examine the prices of "starter" units that tend to be purchased by many first-time homebuyers. As an alternative, the Royal LePage Survey of Canadian House Prices provides detailed house price data by municipality and housing type (see Exhibit 6).

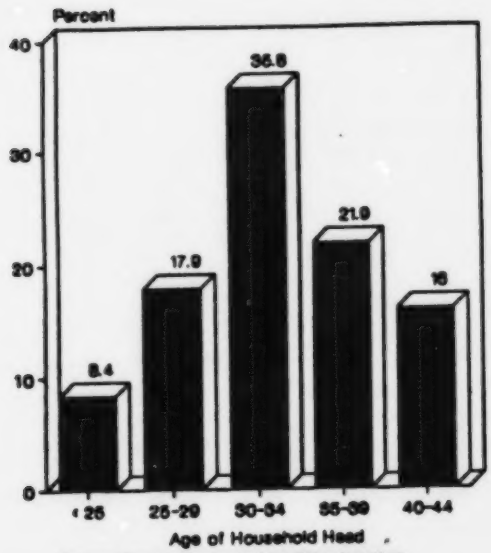
Prices for all types of "affordable" ownership housing (based on April, 1990 data) generally decline with distance from the central core of the Greater Vancouver Area. Homeownership is by far the most expensive in the westside of Vancouver and West Vancouver and most affordable in the municipalities further out, including Surrey, Langley, Maple Ridge, Port Coquitlam and White Rock. A standard two-storey single-detached house on the westside of the City of Vancouver costs $380,000. The same house, however, costs only $150,000 in Surrey and $140,000 in Maple Ridge. The prices at more intermediate locations (Richmond, Burnaby, Vancouver Eastside) are significantly higher than in the outer suburbs - in the $235,000-$275,000 range. Affordable single-detached housing thus are restricted to the locations most removed from the core.

A similar scenario occurs with townhouse prices, except that this type of housing is much more affordable in all locations. With the exception of the city of Vancouver, West Vancouver and North Vancouver, the price of a standard townhouse is under $150,000 in April, ranging from $105,000 in Langley to $159,000 in White Rock. Standard condominium apartment prices follow a similar trend with prices as low as $85,000 in Port Coquitlam and as high as $265,000 on the westside of the City of Vancouver.

The affordability calculations using the MLS average home price show that ownership housing is beyond the means of the average Greater Vancouver Area family. However, the disaggregated Royal LePage data show that a single-detached home can be purchased in the peripheral municipalities (Surrey, Maple Ridge) at a price which is still affordable to many first-time buyers. However, if one works in downtown Vancouver a significant sacrifice in terms of commuting time and costs often must be made, though the recent extension of the Skytrain will ease the necessary sacrifice.

EXHIBIT 7

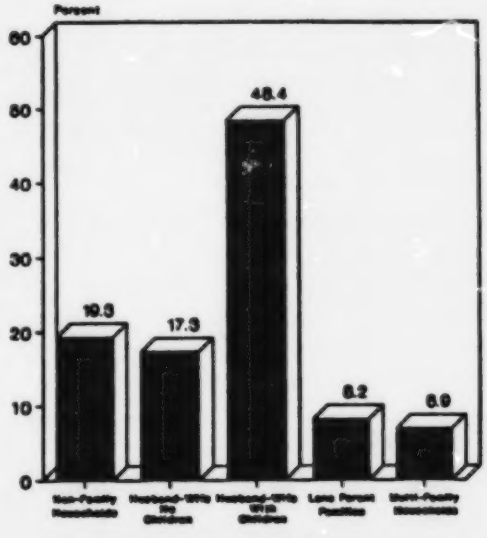
PROFILE OF FIRST-TIME HOME BUYERS
BY AGE OF HEAD, BRITISH COLUMBIA
1984 - MID 1988




Source: Clayton Research Associates based on Statistics Canada 1988 HIFE data.

EXHIBIT 8

PROFILE OF FIRST-TIME HOMEBUYERS
BY HOUSEHOLD TYPE, BRITISH COLUMBIA
1984 - MID 1988




Source: Clayton Research Associates based on Statistics Canada 1988 HIFE data.

EXHIBIT 9

## PROFILE OF POTENTIAL FIRST-TIME HOMEBUYERS BY HOUSEHOLD TYPE AND AGE OF HEAD VANCOUVER, 1990

| Age of Head | Non-Family Households | Husband-Wife Households: No Children | Husband-Wife Households: With Children | Lone-Parent Families | Multi-Family Households | Total |
|---|---|---|---|---|---|---|
| | Number of Households | | | | | |
| <25 | 18,296 | 5,806 | 1,885 | 1,928 | 85 | 28,002 |
| 25-29 | 25,359 | 9,585 | 5,637 | 3,806 | 264 | 44,653 |
| 30-34 | 20,469 | 6,070 | 6,875 | 4,474 | 289 | 38,177 |
| 35-39 | 14,391 | 3,496 | 5,708 | 4,317 | 205 | 28,119 |
| 40-44 | 11,185 | 2,469 | 4,457 | 4,069 | 179 | 22,359 |
| Total | 89,692 | 27,426 | 24,562 | 18,596 | 1,032 | 161,310 |
| | Percent of Total | | | | | |
| <25 | 11.3 | 3.6 | 1.2 | 1.2 | 0.1 | 17.4 |
| 25-29 | 15.7 | 5.9 | 3.5 | 2.4 | 0.2 | 27.7 |
| 30-34 | 12.7 | 3.8 | 4.3 | 2.8 | 0.2 | 23.7 |
| 35-39 | 8.9 | 2.2 | 3.5 | 2.7 | 0.1 | 17.4 |
| 40-44 | 6.9 | 1.5 | 2.8 | 2.5 | 0.1 | 13.9 |
| Total | 55.6 | 17.0 | 15.2 | 11.5 | 0.6 | 100.0 |

Source: Clayton Research Associates based on data from Statistics Canada.

Affordable housing does exist in closer in locations (Richmond, Burnaby, Coquitlam) in the form of townhouses and condominium apartments. The purchase of this type of home may be a necessary first-step for many households to get into the homeownership market in the Greater Vancouver Area.

## 2.2 WHO IS AFFECTED BY THE LACK OF AFFORDABLE HOUSING?

### 2.2.1 The Key Group - Prospective First-Time Homebuyers

Characteristics of households in B.C. who purchased housing for the first time over the 1984 - mid-1988 period are available from Statistics Canada. Similar data are not available for the Greater Vancouver Area so the profile of first-time buyers in B.C. is used as an approximation for the Greater Vancouver Area.

These first-time buyers are concentrated in the 25-39 age group (see Exhibit 7). Three-quarters of first-time buyers in B.C. over the 1984 - mid-1988 period had household heads in this age group. A relatively small proportion of first-time buyers are aged 40-44 years and even fewer have household heads under 25 years age.

Most first-time homebuyers are husband-wife families - more than 60 percent of first-time homebuyers in B.C. (see Exhibit 8). The majority of these are couples with children and many of the currently childless couples are likely expecting to have children in the not-too-distant future. Non-family households, primarily persons living alone, comprise about 22 percent of the first-time buying population while lone-parent and multi-family households are much less likely to purchase a home.

The profile of first-time homebuyers in B.C. shows that most first-time buyers are husband-wife families with heads aged 25-39 years of age. Assuming this is representative of the current Greater Vancouver Area situation a profile of potential first-time homebuyers in the Greater Vancouver Area can be developed.

The definition of potential first-time homebuyers used in this study includes all renter households in Vancouver with heads aged less than 45 years. Thus, there are currently an estimated 161,310 potential first-time buyers in the Greater Vancouver Area, a relatively large pool of prospective buyers (see Exhibit 9). However, more than 50 percent of this pool is comprised of non-family households which are mostly single persons living alone. These households are not likely to be prime candidates for homeownership, as only 17.9 percent of first-time buyers in B.C. over the 1984 - mid-1988 period were non-family households. Thus, singles are probably a lesser concern for government action aimed at enhancing ownership affordability than families with children.

About one-third of potential first-time homebuyers in the Greater Vancouver Area are husband-wife families, with just under half of these households having children. These households are the ones whose access to the ownership market has been restricted the most by the sharply deterioration in affordability. About one in ten

## EXHIBIT 10

### OWNER OCCUPIED DWELLINGS BY REAL DWELLING VALUE* AND MOBILITY STATUS GREATER VANCOUVER AREA, 1981 AND 1986

| 1981 | Stayed in GVA | *Migrants* Within GVA | Within B.C. | Inter-provincial | Inter-national |
|---|---|---|---|---|---|
| Dwelling Value (Owner's only) | | | | | |
| less than 50,000 | 4.6 | 5.0 | 5.8 | 9.1 | 3.6 |
| 50,000 - 99,999 | 9.6 | 10.3 | 12.1 | 10.0 | 6.4 |
| 100,000 - 149,999 | 24.7 | 29.8 | 35.7 | 25.3 | 36.4 |
| 150,000 or above | 61.1 | 54.9 | 46.3 | 55.6 | 53.7 |

| 1986 | Stayed in GVA | *Migrants* Within GVA | Within B.C. | Inter-provincial | Inter-national |
|---|---|---|---|---|---|
| Dwelling Value (Owner's only) | | | | | |
| less than 50,000 | 8.1 | 9.6 | 16.3 | 9.9 | 10.9 |
| 50,000 - 99,999 | 54.2 | 54.6 | 66.7 | 50.5 | 60.0 |
| 100,000 - 149,999 | 24.9 | 24.6 | 13.2 | 25.7 | 16.4 |
| 150,000 or above | 12.8 | 11.1 | 3.9 | 13.9 | 12.7 |

* 1986 values have been deflated into comparable 1981 values.
Source: 1986 Census of Canada.

potential purchasers are lone-parent families but few of these have been candidates for home purchase even when it was much more affordable - their incomes typically are simply too low.

### 2.2.2 In-Migrants Planning to Buy Also Affected

Prospective first-time homebuyers are not the only group adversely affected by the dramatic deterioration in the affordability of ownership housing. Previous homeowners migrating to the Greater Vancouver Area from other parts of Canada and abroad, if moving from areas with lower housing costs, are also affected. The equity that these households have from the sale of a previous home is often insufficient to purchase a comparable dwelling in the Greater Vancouver Area. As a consequence, in-migrant households from lower cost areas must purchase smaller units, locate on the fringe or face significantly higher monthly carrying costs if they wish to become owner-occupiers.

For the first half of the 1980s, owner-occupied housing purchased by in-migrants was generally similar in price to housing purchased by the Greater Vancouver Area population (see Exhibit 10). There are some notable exceptions however. Migrants from within B.C. tended to purchase lower-priced dwellings as did international migrants although to a lesser extent.

The rapid deterioration of homeownership in the Greater Vancouver Area has been a fairly recent phenomena (since 1987) and the 1986 Census data are not fully representative of the current situation. The sharp increases in resale prices over the past four years have not been national in scope. Home prices in both the Greater Vancouver Area and Toronto have increased dramatically relative to those in other major urban centres in Canada. Therefore, there is little doubt that, except for migrants from southern Ontario and, perhaps, some international migrants, the dramatic reductions in the affordability of homeownership since 1986 have had a significant negative impact on this group of households as well.

### 2.2.3 Move Up Buyers Really Not Affected

Two groups of households affected by the ownership affordability problem have been identified, first-time homebuyers (particularly husband-wife families with and without children) and in-migrants from lower housing cost areas. A third group of households generally not adversely affected by the affordability problem are move-up buyers. The recent sharp increases in resale house prices translate into an increase in equity for these households and therefore it is unlikely that their ability to "move-up" to more expensive housing has been constrained. In fact, the recently buoyant real estate market in the Greater Vancouver Area benefited many move-up buyers significantly since the increased demand for all types of ownership housing made it easier for these households to sell their homes quickly.

The fact that move-up buyers have generally not been adversely affected by the recent deterioration of ownership affordability helps to explain the recent behaviour of builders of new housing. The Greater Vancouver Area new house market to date this year has largely targeted on move-up buyers. Evidence of this comes from the recent Pulse Survey of Canadian homebuilders[1]. Only 5 percent of Vancouver builders in the Greater Vancouver Area stated their intention to pursue first-time buyers as their major customers in 1990. Thus, first-time buyers generally will have to purchase resale houses or condominiums.

## 2.3 RAMIFICATIONS

What are the consequences of the recent sharp deterioration in the affordability of ownership housing? The lack of affordable ownership housing has a number of ramifications for other sectors of the local economy, both housing and non-housing.

Households must have shelter. With ownership housing so unaffordable this shelter is increasingly found in rental housing. Current potential homebuyers in the Greater Vancouver Area are being forced to delay the transition to homeownership and more in-migrants rent as they are unable to purchase a home. Both of these reactions to the current affordability problem put more pressure on an already tight rental market, thereby increasing the costs and reducing the choice of housing for renters in the Greater Vancouver Area, which puts added pressures on low income renters.

The recent surge in the prices of existing homes, coupled with the strong desire of households to be homeowners, is leading to increasing market pressure for smaller new houses to be built on smaller lots as well as for more higher density ownership housing. These pressures for more affordable and higher density housing have been met with increasing community opposition (the NIMBY problem).

The price of housing generally falls with distance from the central core and is therefore cheapest in the peripheral municipalities. The lack of affordable ownership housing in the core municipalities has led to increased demand for housing at the urban fringe, particularly in municipalities like Surrey which still have a large potential capacity for new housing. The sharp increase in growth of urban fringe communities is of great concern to these municipalities and has resulted in the advocation of "managed growth" policies.

Homeownership in the Greater Vancouver Area is far less affordable then in other major urban centres across Canada. This is beginning to discourage in-migration of both labour and retired households. Less in-migration results in a further shortage of labour, thereby increasing the costs of doing business in the Greater Vancouver Area and, ultimately, will lead to slower economic growth in the region.

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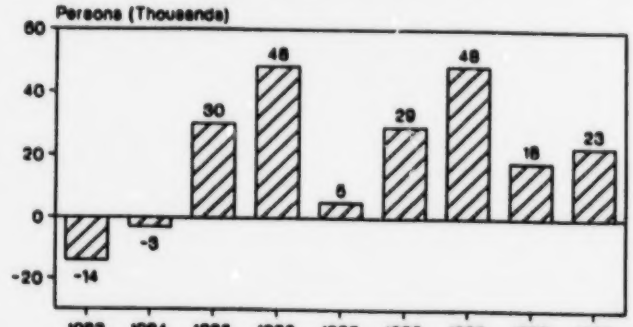
[1] Source: Survey conducted by Clayton Research Associates on behalf of Fiberglas Canada and the Canadian Home Builders' Association in January, 1990.

## EXHIBIT 11

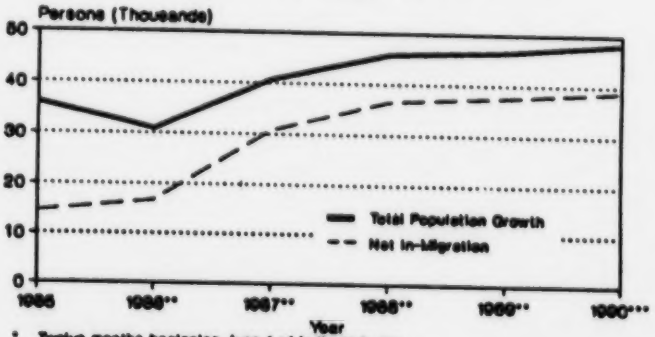
### GROWTH IN EMPLOYED LABOUR FORCE* GREATER VANCOUVER AREA




* Growth over previous year.
Source: Statistics Canada.

## EXHIBIT 12

### POPULATION GROWTH AND MIGRATION* GREATER VANCOUVER AREA




* Twelve months beginning June 1 of indicated year.
** Estimate.
*** Forecast.
Source: CMHC.

## 3.0 UNDERLYING CAUSES OF THE AFFORDABILITY PROBLEM

This section provides an analysis of the causes of the ownership affordability problem in the Greater Vancouver Area. The analysis addresses three questions:

- Why have home prices increased so rapidly since 1987?
- Why is the supply of serviced land not more responsive to changes in demand? and
- Are there forces which are contributing to a long term rise in serviced land prices?

### 3.1 WHY HAVE HOME PRICES INCREASED SO RAPIDLY SINCE 1987?

The simple answer as to why home prices have advanced sharply is that the demand outpaced the supply. But this begs to question why the demand increased so rapidly and why the supply failed to keep pace.

On the demand side, both the ownership and rental sectors of the housing market in the Greater Vancouver Area have been characterized by strong demand pressures since 1987. They share common underlying causes.

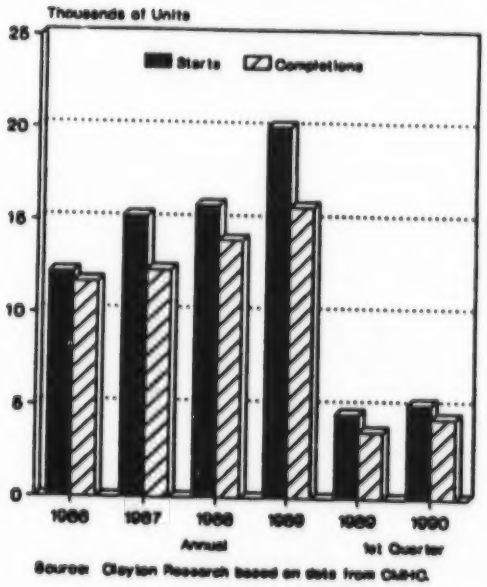
The Greater Vancouver Area economy experienced a marked turnaround in 1985 following several years of actual losses in its job base (see Exhibit 11). The recovery in the U.S. housing market and the construction of Expo contributed to the recovery. Contrary to the consensus at the time, the economy remained strong in 1987 after Expo though there was a pause in job creation. Then, employment growth surged in 1988 and again in 1989.

This resurgence in economic fortunes attracted the attention of job seekers from other parts of Canada as well as from abroad. The result has been an explosion in net migration to the Greater Vancouver Area (commencing in 1987) (see Exhibit 12). The bulk of these migrants came from other provinces and countries (i.e., not from other parts of B.C.).

While the demand for ownership housing initially came largely from purchasers intending to live in their units, rising prices and the prospect of future price hikes attracted investors and speculators into the market. Even buyers intending to occupy the homes they purchase move up their decision to buy to get into the market before prices rise even more. Moreover, since many move up buyers bought new homes not yet built this component of demand is temporarily inflated until the purchasers put their existing home onto the market.

**EXHIBIT 18**

**STARTS AND COMPLETIONS OF UNITS INTENDED FOR OWNER-OCCUPANCY GREATER VANCOUVER AREA**




Source: Clayton Research based on data from CMHC.

The stock of ownership housing cannot be expanded rapidly. The primary source of additional ownership housing is the construction of new single-family and condominium apartment dwellings. Even though the quantity of new ownership housing built in the Greater Vancouver Area has increased sharply since 1986, the increment to the total stock of owner-occupied housing remains relatively small - less than 6 percent per year (see Exhibit 13).

Even though this supply of new ownership housing has been augmented by the conversion of existing rental structures to owner-occupancy, these additions to the housing stock were not sufficient to prevent a marked rise in home prices.[2]

Why has the amount of new housing built in recent years not been even larger given the conditions of extremely strong demand? The primary reason is that two important factors of production (labour and land) have been in short supply.

A shortage of labour is not as serious as a shortage of serviced land since higher compensation (wages, bonuses, etc) attracts additional supply (through overtime, migration of construction workers to the Greater Vancouver Area). An increase in the supply of serviced land onto the market is largely in the hands of municipalities.

## 3.2 WHY HAS THE SUPPLY OF SERVICED LAND NOT INCREASED MORE?

### 3.2.1 Myopic Expectations

When the demand for new housing is low, as it was in the early 1980s following the recession, both developers and municipalities expect it to remain that way; they have myopic expectations. Hence infrastructure expansion, approval requests and other municipal activities are all in low gear. Therefore, when the unexpected net migration expansion and subsequent surge in the demand for land for new housing occurred, the developers and municipalities were not ready. That is, neither local governments, builders nor developers foresaw the coming huge increase in demand. As a consequence, municipalities were overwhelmed with approval requests and demands for new infrastructure. This is not to blame the municipal governments; it was unforeseen by everyone.

### 3.2.2 Inherent Lags

There was also a recognition lag. Has demand really increased? If so, for how long? Once the perceived surge in demand is recognized then approvals for new

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[2] It is estimated that 2,000 existing units on average are being converted annually from renter to owner-occupancy in the Greater Vancouver Area in the current 1986-1991 period. See Recommendations for an Affordable Rental Housing Strategy, April, 1990 prepared for the GVRD by Clayton Research Ltd and CitySpaces Consulting Ltd.

developments must go through the approval process. Approvals and construction of urban infrastructure take time - land cannot be brought into use overnight.

The time to obtain approvals is relatively long due to the differing agendas of municipalities and developers. Builders and developers are primarily driven by the profit motive. They therefore have a vested interest in getting land on the market when expectations are for higher prices in the future. Municipalities, on the other hand, are guided by the political process. They are worried about how potential developments will impact on their finances and how their constituents feel about potential development and the pace at which it proceeds (i.e., the impact on the tenure of their jobs).

The approval process has become increasingly more complicated due to community opposition (NIMBY), and this contributes to the sluggish response of the land supply. The deterioration of homeownership affordability has increased pressure for smaller homes on smaller lots and higher density developments. Frequently, local residents view this "affordable" housing as detrimental to their communities. Environmental concerns are also adding to the time it takes to bring serviced land onto the market.

### 3.3 ARE LONG-TERM LAND PRICES RISING?

The recent surge in resale house prices in the Greater Vancouver Area is primarily a result of a huge increase in demand relative to a supply that is essentially fixed over the short-run. The supply side of the housing market is not very dynamic in the short-run. However, although not entirely responsible for the inflationary boom, municipal regulations and community "selfishness" have exacerbated the situation by restricting the supply of serviced land.

A distinction must be made between short-run price increases and long-run price levels. Over the short-term, demand is the primary force driving the ownership housing market. However, over the longer term, the market outcome is the result of the interaction of both demand and supply. Thus factors affecting the supply of land and housing affect the affordability over the long-term.

Increasingly, the supply of serviced lots has been reduced as a consequence of municipal financial requirements and regulations, which are aimed at generating revenue or reducing current and future costs for the municipalities. This behaviour on the part of municipalities, by restricting the supply of serviced lots or directly adding to their cost, ultimately must affect the affordability of new housing. And by restricting the supply of new housing, the price of existing housing increases as well.

Examples of financial requirements and regulations imposed by municipalities include: development cost charges, planning approval processes, excessive standards and donations of land for parks and schools. These costs and requirements all add to the cost of bringing serviced land onto the market. They thus exacerbate the

current short-term affordability crisis and will cause deterioration in the affordability of homeownership further down the road.

In summary, then, the primary cause of the recent market reduction in the affordability of ownership housing in the Greater Vancouver Area has been the resurgence of the regional economy. This has been exacerbated by the rise in interest rates and the sluggish response of land supply to the surge in demand.

# 4.0 OPTIONS FOR ATTACKING THE OWNERSHIP AFFORDABILITY PROBLEM

The relative merits of various actions targeted at enhancing the affordability of ownership housing are considered here.

## 4.1 OPTIONS TARGETED AT DEMAND/SUPPLY IMBALANCE

As noted previously, the marked rise in home prices in the Greater Vancouver Area since 1987 originated from a resurgence in the demand for housing resulting from a strengthening economy. Rising prices are a normal market response to a shortage. Thus, rising prices in a market economy act as a trigger to developers and builders to increase the supply of new ownership housing. They also encourage owners of existing rental structures to consider converting their buildings to ownership-occupancy to maximize their returns.

To suppress these rising prices by instituting some form of controls would be counterproductive. The fact is that the more prices rise, the quicker and more substantial will be the private sector supply response to the shortage.

It would appear that the Greater Vancouver Area ownership housing market is no longer characterized by a supply/demand imbalance. The escalation in prices together with the recent rise in interest rates has increased supply and diminished demand to the point that the market at present has moved from a shortage of supply to some oversupply.

### 4.1.1 Homebuyers' Subsidies

Subsidies to homebuyers, whether in the form of interest or downpayment assistance, to all buyers, or restricted to particular groups (e.g., first-time buyers) at a time there is an overall shortage of ownership housing would simply aggravate the shortage. By stimulating demand at a time demand is already buoyant, subsidies would add to the pressures pushing prices up.

### 4.1.2 Tax on Investors/Speculators

A tax on investors (someone buying and putting the home on the rental market) and/or speculators (someone buying with the intention of selling the home before it is occupied) purchasing new or resale ownership housing has merit during a period of demand/supply imbalance since it would reduce a component of the demand for ownership housing in a rising market - demand from purchasers not intending to become owner-occupants. This should act to moderate rising prices. The type of tax

usually advocated is to tax the gain at the time of sale by investors and speculators at a hefty rate.

It should be realized that the purchase of homes by investors adds units to the rental stock until such time the investors decide to sell. Any tax which discourages investors in a rising market will reduce needed additions to the rental stock. One way to minimize such conflicts would be to tie the rate of the tax to the length of time an investor/speculator owns the property - the shorter the holding period, the higher the rate. The tax could work in a way similar to rear loading charges for mutual funds. After a period of time (say five years) there would be no tax incurred on the sale. This would penalize speculators but not longer term investors providing rental housing.

Timing is crucial for the implementation of such a tax. It has to be introduced in the early phase of a rising market. Since the period of rapid home price increases in the Greater Vancouver Area appears to be over, it is not an action that will help enhance affordability at the present time.

The provincial government would appear to be the best level of government to introduce this form of tax since it would have to be applied to the province as a whole or entire regions which are experiencing a demand/supply imbalance.

### 4.1.3 Allow Condominium Conversions

The conversion of existing rental buildings to owner-occupancy is a method of expanding the stock of ownership housing. And since the prices of converted units in older buildings will almost always be less than condominiums in new buildings in comparable locations, the converted units will be more "affordable" than the new units.

As noted previously, there have a considerable number of rental units converted to owner-occupancy in recent years. Most of these conversions have been in the tenure of the occupied units rather than in the legal status of the buildings. The buildings were strata titled at the time of construction. For rental buildings not strata titled, conversions have been limited by municipal policies. These latter buildings which predate the latter 1970s could be an important source of "affordable" ownership housing.

The downside of allowing large numbers of conversions in a buoyant market is that this would worsen the accommodation problems of low income households and impose social costs on longer-term residents who could not afford or did not want to buy the unit they occupy. An interesting aspect of conversions occurs to the extent that renters who had no intention of buying a home buy a converted unit. Since these purchases would reduce both the demand and supply of rental accommodation by the same amount, the net effect on the rental market would be nil.

Actively encouraging conversions a time when both the ownership and rental markets are very tight would not be a very sensible initiative. While the supply of ownership housing would be expanded, this would largely be at the expense of the rental market.

## 4.2 OPTIONS TARGETED AT ENHANCING HOME BUYERS' ABILITY TO PURCHASE

The bulk of first-time home buyers in the Greater Vancouver Area have a dual problem: insufficient financial resources for the downpayment and insufficient income to carry the mortgage and other ongoing costs of the home purchase. A solution to these problems would be grants from government to first-time buyers. The federal Assisted Home Ownership Program introduced in the 1970s is an example of a grant program intended to help renting households on the margin of affordability to become homeowners. This program provided either interest free loans or grants to purchasers of moderately-priced new homes. Several provinces, including British Columbia, provided supplemental assistance to the federal program.

Another type of grant program was the Canadian Home Ownership Stimulation Program in the early 1980s which provided $3,000 grants to all purchasers of new homes and first-time buyers of existing homes. The program was intended more to stimulate new homebuilding rather than to promote affordability.

With the magnitude of the affordability problem in the Greater Vancouver Area, a program of grants which could make a serious contribution to the affordability problem of prospective first-time buyers would be extremely costly. These costs would certainly be beyond the means of municipalities in the GVRD to fund.

The affordability problems of first-time buyers in the Greater Vancouver Area are largely the product of high home prices though high interest rates are aggravating the problem. It is unlikely that either the federal government or the province would consider a program of grants to first-time buyers in the Greater Vancouver Area only. Such a program would not do anything about the current high price structure of homes. Only if the economy were to move into a serious recession is it likely that the senior governments might introduce a program to temporarily stimulate the housing sector.

The solution to high mortgage interest rates is to reduce inflationary pressures and improve productivity in the Canadian economy. Subsidies to homebuyers to cushion the influence of these high rates should be a measure of last resort if rates go even higher and if it appears that they will remain there for an extended period.

Since subsidies to homebuyers per se would do nothing to reduce the price level of ownership housing, the research for meaningful options for dealing with the affordability problem shifts to the supply side of the housing marketplace.

## 4.3 OPTIONS TARGETED AT ENHANCING THE OVERALL SUPPLY OF OWNERSHIP HOUSING

There are two ways to expand the supply of "affordable" ownership housing. The first is to increase the overall supply of ownership housing sufficiently to keep prices from rising or, perhaps, to cause some reduction in average prices. The second is to boost the share of the housing being added to the ownership housing stock which is "affordable". This section explores the first approach.

### 4.3.1 Increase the Supply of Serviced Land for New Housing

A fundamental problem in the Greater Vancouver Area over the past three years is that the supply of serviced land has not kept pace with the demand. While the problem seems obvious, solutions are much more complex.

One of the first things that has to be determined is whether the shortage of serviced land is a temporary or longer-term phenomenon. Similar shortages emerged in the 1979-1981 period but the buoyant market conditions of the time resulted in considerable land coming onto the market, albeit with a lag. The combination of more available serviced land and a recession-induced drop in housing demand resulted in a sharp drop in average home prices in 1982 followed by fairly stable prices for several years after. Will this scenario be repeated this time around?

To some extent, the same pressures are resulting in more land coming to the market. However, there seem less willingness on the part of municipalities to accept growth automatically than was the situation in the 1979-1981 period. Moreover, few, if any, observers are anticipating a downturn in the Greater Vancouver Area economy of the severity of the downturn in the early 1980s. Hence, it appears likely that home prices will stabilize at or close to the current high level. Especially if interest rates decline over the next two or three years, affordability will gradually improve. However, the fact remains that many prospective first-time buyers will be unable to get into the ownership market who would have been able to if affordability had remained at pre-1987 levels.

A determined effort on the part of both the private sector and governments to increase the overall supply of serviced land will reinforce these basic market forces and enable more residents of the Greater Vancouver Area to become homeowners in the coming years. How can this be done? What are the options?

- Designate/zone substantially more land for housing.

  The suburban municipalities are the key to a sizeable increase in the amount of land available for new housing. While more central municipalities can also increase the supply of land for housing (e.g., by redesignating obsolute industrial land), the resulting housing would

typically be higher density and expensive (at least on a square foot basis). Most families wanting to enter the ownership market are likely to be strracted to low-density, suburban housing.

Suburban municipalities in recent years have, in general, become more reluctant to designate or zone more land for housing. They are increasingly concerned about the impact of rapid growth on the breadth and quality of services provided to existing residents and the financial consequences of growth. These are concerns that have to be dealt with if the land supply is to be opened wider.

- A commitment to long-term anticipatory planning.

The economy and the demand for housing are cyclical. They always have been and will continue to be in the future. Unfortunately, the exact timing and extent of each upturn cannot be predicted consistently with any degree of accuracy. Therefore, municipalities often are not prepared for the upturn when it occurs. In fact, when economic activity is not buoyant, complacency often sets in. Why add to sewer and water trunk facilities, extend roads or build a new school or recreation centre when the demand pressures are minimal? So these community infrastructure extensions are deferred. This compounds the problems that emerge when the economy and housing market recover. The lack of available infrastructure capacity restricts the supply of land adding to the upward price pressures for homes.

The need for long-term planning, for both the amount of land required for new housing and the required infrastructure, is being increasingly recognized in other jurisdictions.

The City of Calgary has had a long term planning perspective for many years. The province of Ontario under its Land Use Planning for Housing Policy Statement calls on municipal governments to: (a) designate sufficient land for housing to maintain a 10 year supply at all times within a 20 year planning time frame; (b) identify the projected servicing needs for these lands in their official plans; and (c) maintain at least a three year supply of draft approved and/or registered lots for new housing at all times.

Long-term planning in an urban region cannot be done by each member municipality in isolation. A regional body is required to undertake regional plans and to coordinate and, if necessary, coerce local municipalities into action.

- The financing of infrastructure.

The burden of financing infrastructure extensions and improvements falls mostly on suburban municipalities who have the least ability to pay. Lacking the commercial and industrial tax base of more central municipalities, these municipalities are searching for alternative ways to

fund this needed infrastructure without imposing excessively large tax loads on their existing residents.

Municipalities a long time ago shifted the costs of services internal to a subdivision to developers. These costs have become embedded in the price of the serviced land. In more recent times, there has also been a shift in the financial burden associated with growth-related capital costs outside specific subdivisions to developers. The **Municipal Act** in B.C. allows municipalities to levy development cost charges to pay for the capital costs of sewer, water, drainage and highway facilities and parkland acquisition to service, directly or indirectly, the development for which the charge is being improved.

Ontario has recently formalized and extended the ability of municipalities to shift infrastructure costs to land developers. Under the **Development Services Act, 1989** municipalities and school boards can levy charges for growth-related capital costs. In addition to the hard services charged in B.C., buildings, rolling stock, furniture and equipment and library material are eligible capital costs.

Over the long-term much of these costs are reflected in the price of serviced land and, subsequently, in the price of new homes. The increased use of development cost charges is at odds with the objective of making housing more affordable.

There is a need to find options to the increased use of development cost charges to fund infrastructure if more serviced land is to be brought to the market at a price which is compatible with the goal of increasing the supply of homes. Possible options include:

- Within the existing fragmented political structure of the Greater Vancouver Area, to have the province fund the capital costs of "big-ticket" municipal infrastructure items such as sewer, water and roads; or

- Pool commercial and industrial assessment within the Greater Vancouver Area and redirect tax revenues to suburban municipalities willing to make considerable serviced land available for new housing. This could be superimposed on the existing municipalities by the province or through a reorganized political structure within the GVRD which gives the GVRD responsibility and tax resources to undertake infrastructure improvements and extensions.

## 4.4 OPTIONS TARGETED AT ENHANCING THE SUPPLY OF AFFORDABLE OWNERSHIP HOUSING

Government has the power not only to enhance ownership affordability by expanding the supply of serviced land relative to the demand but to expand the share of housing coming on to the market which is affordable. There are a variety of options here.

### 4.4.1 Increase Intensity of Land Use

The costs of new ownership housing is very much influenced by the cost of serviced land. Initiatives to increase the number of homes per acre can make an important contribution to producing more affordable housing. This can be done in several ways:

- Reduce lots sizes for single-detached houses.

  Lots for new houses in the Greater Vancouver Area typically are 50 front feet or larger. These are considerably larger than in Toronto where lots with 30 to 40 front feet have become the norm. In the early 1980s in Calgary and Edmonton, when land costs were very high, the sizes of lots also were often quite a bit smaller than the current sizes in the Greater Vancouver Area.

  Allowing builders to build on lots as small as 3,000 square feet (30 by 100 feet) would be a major step forward in producing more affordable new houses.

- Allow more semi-detached and townhouse units.

  Increasing the proportion of semi-detached and townhouse units in subdivisions would have essentially the same type of effect on the final cost of new housing as reduced lot sizes for single-detached houses.

- More innovative land use configurations.

  Clustered housing is a concept whose time has come. By having flexible setbacks and sideyards low density forms of housing can be placed on a parcel of land that, at the same time, provides a better living environment and higher densities than a conventional subdivision of single-detached homes. There could be servicing cost savings too as a result of narrower streets (which would be owned by the homeowners) within the development than conventional municipal streets.

### 4.4.2 Letting the Market Work Versus Dictating Higher Densities

Builders and developers build the types and forms of new homes that buyers want to buy. Recently, virtually all new home buyers have been repeat buyers. These buyers typically want larger homes loaded with amenities. To the extent first-time buyers are in the market, they have been buying the lower priced existing homes sold by the repeat buyers.

Market conditions have now changed as they did in the Greater Vancouver Area in the early 1980s and in Toronto over a year ago. Builders increasingly will be realizing that to sell homes they have to reorient their product and their marketing to first-time buyers. This will mean smaller homes on smaller lots with fewer amenities. They will do this in order to remain profitable in a more competitive market.

The role of municipalities in this market environment is to respond quickly to developer requests not only for more land to be approved for housing but also for higher densities and innovative land use configurations.

In some respects, the province of Ontario has gone a step further than what is suggested above. It is requiring municipalities to plan for housing forms which will ensure that a minimum of 25 percent of the new housing units built in the municipality are "affordable". This affordable housing is to be distributed throughout a municipality. The maximum price range for affordable housing varies by urban centres. In the Toronto area, the price ceiling is approximately $156,000.

The Ontario approach has a number of limitations. Probably the most serious are that it does not deal with the root problem, has no direct enforcement mechanism and is rigid. The root problem is a lack of resources for funding infrastructure in assessment-poor suburban municipalities. Without dealing with this fundamental issue in a meaningful way, municipalities have no incentive to readily respond to the province's initiatives. Moreover, there are no explicit penalties for municipalities not responding fully to the initiatives. Finally, by dictating the forms of new housing, there is a danger of market distortions in the future.

#### Linkage fees

Some municipalities in the United States are requiring the developers of new commercial projects to contribute to an affordable housing fund. Without going into the merits of such charges, they seem more appropriate for low-income rental housing than for ownership housing.

#### Condominium conversions

As noted previously, the conversion of existing rental buildings to owner-occupancy is a source of more affordable ownership housing. Therefore, there are stronger arguments in favour of allowing conversions, with appropriate controls, than to

prohibit conversions. There should, however, be municipal policies to provide protection for both tenants and buyers.